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General Business Conditions

THE business situation during May, as in April, has been dominated by the general disposition to shorten commitments, reduce inventory, and wait for lower prices. Hopes that seasonal influences might check the recession have been disappointed. It would be too much to say that no Spring improvement has occurred; building figures show a good upturn, and the opening up of outdoor work has had a pronounced influence in maintaining employment. But the effects of these gains have been lost in general buying slackness and industrial price weakness. Distributors are trying to carry as little stock as possible, counting on manufacturers for prompt deliveries. Manufacturers in turn are trying to avoid a pile up of finished goods and to get along with a minimum of purchased materials. Thus new orders are reduced all along the line. The drop is cumulative as it reaches back into the basic industries, and activity suffers. That is the chief explanation of the present dullness.

Consumers also have inventories, and their disposition to buy also fluctuates, as is now being demonstrated by declining sales of new homes and household equipment. People choose to wait for lower prices, once urgent needs are satisfied, or they choose to save rather than buy at all. However, reduction of consumers' spending is far less a factor in the recession than reduction of business spending. Department of Commerce figures are available on total personal expenditures through the first quarter of 1949, and on all retail expenditures for April. They indicate that the seasonally adjusted annual rate of personal expenditures, after dropping from December to January, has since held level (April in fact showed a slight upward trend) at about 2½ per cent under the average for the fourth quarter of 1948, and 2½ per cent above the first quarter of 1948. These are dollar totals, and the price trend has been downward.

With all the allowances and qualifications which people may wish to apply to these figures, they indicate that final consumption has been well maintained, and that those who look no further than the drop in manufacturers' orders see things worse than they are. Preliminary reports suggest that personal expenditures in May have not varied markedly from the April level.

Plant and equipment expenditures continue large. But the momentum has slackened, and both manufacturers of capital goods and the primary producers who supply them report new orders slow. In many of these lines backlogs are running down.

Industrial Output Dropping

As backlogs decline, industrial activity continues to recede. The Federal Reserve Board's index of industrial production for April was 179 (1935-39 = 100) against 184 in March and the peak of 195 last October and November. May evidently has brought a further decline. The steel mill operating rate has dropped during the month from 97½ to 92 per cent of capacity. It seems plain that steel has now run into the same conditions which hit the non-ferrous metals earl-

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ier; steel orders are dropping not only because sales of many things made from steel are falling, but because steel users want to keep down inventory. Automobile assemblies have been reduced by the Ford strike and by temporary difficulties of other manufacturers due to strikes in supply plants. Further cutbacks and layoffs have been made in household equipment and appliance lines. No definite sign of a turn has appeared in the textile industries, in which curtailment has been severe for a considerable time.

Employment in manufacturing industries is dropping, and shortening of hours also takes something out of pay envelopes. But in overall employment a rise running through the Spring occurs in all but the most adverse circumstances, and even this year is no exception. Probably this will be accompanied by an increase in unemployment also as schools let out and the labor force expands. The real test of employment will come in the Fall when farm work, construction and the like enter their seasonal declines. Then the condition of the industries will govern.

Shortening of Inventories

A business recession which is chiefly attributable to "catching up" has in itself elements of a spiral, because a drop in buying leads to industrial curtailment, reduced employment and loss of purchasing power. But it also supplies its own brake to such a spiral, for the decline in orders and production inevitably exceeds the drop in ultimate consumption, and in due course will reverse itself. Reduction of inventory is making fast headway, and it is hard to see how commitments can be shortened further. Department stores' commitments have been cut by a third in the past year. Their stocks of merchandise are well below a year ago. The National Association of Purchasing Agents says that 62 per cent of its members are on a hand-to-mouth to thirty-day buying basis, and that inventories of purchased materials dropped sharply in both April and May.

Copper statistics also provide a striking illustration of current trends. There is no statistical measure of the final consumption of copper, but in view of high activity in utilities, automobiles and general construction — which take three-fourths of the copper used — the decline so far probably has been quite moderate. But shipments of copper products by fabricators dropped from 126,700 tons (copper content) last October to 65,454 in April, or nearly half. New orders received by fabricators dropped from 105,317 tons in October and 118,822 in December to 37,387 in April; shipments of copper by producers dropped from 112,580 tons in October to 76,127 in April; new orders received by producers are estimated at only 21,475 tons in April, and May appears to have been an equally dull month. These figures show that processors and distributors are cutting stocks drastically. Eventually they will have to start buying what they use.

Supports for Weak Spots

Every business decline, however, holds elements of danger more severe than inventory correction. Falling prices and falling property values have a depressing impact, failures and losses occur, and purchasing power in those areas is reduced or destroyed. One danger is that weak spots may exist where severe and cumulative liquidation may develop.

This aspect of the situation has been under widespread study, and with respect to the weak spots that have deepened and widened past business declines, most people find the answers reassuring. In 1920 farm land speculation based on debt was a weak spot. Excessive inventory accumulation on borrowed money, for purpose of resale rather than use, was another. Neither of these is present in dangerous degree, and stock market debt, one of the complicating factors in 1929, is negligible. The urban mortgage debt inflation which was an element in 1929 has occurred again this time, but with two considerable differences. One is that a substantial part of the debt is guaranteed by federal agencies, and another is that it is subject to regular amortization. Federal guarantees will not protect borrowers who become unable to carry their property from loss in falling markets, but they will protect and support lending institutions, which in last analysis means savings depositors and insurance policyholders.

Over and above government guarantees, the banking system has a strength and liquidity which is the strongest assurance against a repetition of the contagious distrust and paralysis of credit, and the liquidation due to fear, which dominated the great depression. Money is freely available to good borrowers at low rates, and monetary policies are designed to aid and support business.

Another source of trouble in the past has been the decline in the liquidity of business and individuals, resulting from increases in debt. When short-term liabilities are excessive, and when cash is short and assets cannot be sold to pay debts without severe loss, business and people are in trouble. But cash and cash equivalent assets of the economy now — including $52 billions of redeemable U. S. Savings Bonds held by individuals — are immensely larger than before the war, and have grown much more than personal and business debts have grown. These assets

are reserves of purchasing power for those who hold them. Together with corporate reserves against inventory loss, they strengthen the general situation immensely. Farm price supports, unemployment compensation insurance, and the E.R.P. support of exports are also additional cushions and props.

Where is the Situation Vulnerable?

These elements of strength have been widely discussed and recognized. On the other hand, weak spots are almost sure to appear, and not all will have been foreseen. It is a military truism that generals always fight the last war. Business history can be examined, the weaknesses which have prolonged and deepened past recessions can be searched out, and people can profit from these lessons. Nevertheless, business men wonder what other weaknesses persist, to be disclosed by events.

One weakness may be inherent in a highly developed economy. The will to spend vastly affects demand, and it takes on increasing influence as the standard of living rises far above a subsistence level and people are able to time their buying at their pleasure. Never before has such a high percentage of durable goods, for which demand can be postponed, entered into daily purchases. Many more people have a choice between spending now or waiting than has ever been the case in any other country, or even in the previous history of this country.

A second element of concern is the fact that a considerable number of people have entered business during the postwar years without the necessary capital, experience or ability to make a success. Also, small businesses, which branched out under the impetus of war work, have naturally sought to keep up their volume and maintain a foothold in new lines. This has happened at a time when the tax system has made capital for this type of enterprise scarce and difficult to get. Many new and overgrown concerns may prove to be short of resources to support the impact of declining prices and values. In this area business difficulties are developing. Every such case causes loss and imparts shock.

A third cause of concern is the high break-even point established by the cost increases of the inflation period, and the fear that these costs, which in last analysis are largely wage costs, will prove too rigid to permit the break-even point to be brought down as volume declines.

Problem of Price Adjustment

It is natural that business men should be trying to foresee the future, and to estimate how long and how far the current decline may go. Everyone should realize also that neither the time nor the extent of the drop is foreordained. Both will be greatly influenced by the policies that are followed, and by the degree in which people face and deal with problems of recovery.

In all likelihood it will turn out that the most troublesome problem raised by the recession is the problem of price adjustment. Potential buyers of many consumers' goods, particularly of the durable kind, have now satisfied their most urgent wants, price is again a consideration, and lower prices are needed to uncover a new layer of demand. Business men who are expecting price cuts will continue hand-to-mouth buying as long as that expectation dominates. Farmers have had a sharp decline in prices of many of their products, and although farm prices had risen much more than most industrial prices, farmers feel rightly or wrongly that the cost of the things they buy must come down also.

The industries are caught between this attitude of buyers and their own burdens of rigid wage rates, declining volume and increasing ratios of sales and overhead expense. Many will think the problem beyond their power to solve. Nevertheless, declining sales will force lower prices, through the effects of competition, and the business which recognizes this and cuts its cloth to fit, as far as lies in its power, will contribute most to recovery.

Fortunately the cost outlook has favorable as well as unfavorable elements. The 1948 peak in prices of basic materials was held for a comparatively short time, and prices of many materials have dropped. Prices of some others will drop further when new crops come in. Declines in basic commodities are being passed along to consumers of finished goods in encouraging fashion. Costs are reduced by inventory cutting, by abundant supplies and prompt delivery of materials, by elimination of the inefficiencies, the roundabout shipments and extraordinary conversion costs, the gray and black markets which accompanied the boom.

As the labor market changes from a tight to an easy position, and as the benefits of the huge plant and equipment investment of the past two years are realized, individual output should be expected to increase. Greater productivity will reduce costs without cutting wage rates. There is evidence that such a trend is already under way and making good progress. Whatever the outcome the need is clear. If labor and management together can increase man-hour output and reduce unit labor costs to bring down prices to the lower levels which buyers now demand, break-even points can be reduced.

The Wage Question

It follows from the foregoing that the most harmful influence which could possibly be injected into the situation would be another round of wage advances, which would raise industrial costs and make the necessary adjustments in industrial prices impossible. Advances in wage rates heretofore have had an inflationary effect. They came at a time when people and pipelines were short of goods, when incomes of farmers were steadily increasing, and when higher costs and prices could be readily passed on. Now the daily reports of business show that the markets for both goods and labor have changed, and farm incomes are declining. Increases in wages, costs and prices under current conditions would curtail sales of goods, and hence production and employment. The real interest of factory workers is in maximum production of the things they use and maximum employment for themselves, not in higher money wage rates which lead to disruption of the exchange of goods between them and other groups of the population, and thus to idleness.

Many people have lived under illusions during the inflationary period, and now have realities to face. The volume of business was abnormal for a time, because demand was swollen to fill accumulated scarcities and empty pipelines. Now that is over. The job of business is to adjust to lower price levels and more competitive conditions, with greater attention to turning out goods better and cheaper. Industrial workers generally and farmers as well have had not only the highest money wages, but the highest real standards of living that have ever been known in this or any other country. They can be preserved under the conditions that now present themselves, but only by higher productivity, to reduce costs and keep the price structure in the balance that is necessary if trade and investment are to go on.

Credit Developments

The decline in production, trade, and prices, and slackening off in private capital outlays, have had their natural counterparts in the money and capital markets. Bank loans have fallen off substantially since the turn of the year. Corporate bond flotations and real estate mortgage financing, though still very active by pre-1948 standards, are down from the record rate of last year. While dampened by Federal Reserve sales of governments, and expectations that the Treasury may enter the market to borrow during the Summer, the bond market has had a strong tone.

The Federal Reserve Board, recognizing the change of environment, has made a succession of moves designed to ease some of the restraints on the supply of credit which had been clamped on in 1948 or earlier. Consumer credit regulations, put back into force last August under emergency legislation, were relaxed somewhat on March 7. Margin requirements on listed stocks were lowered from 75 per cent of market value to 50 per cent on March 30. Consumer credit regulations were further eased April 27. Effective May 1-5 the Board partially rescinded 1948 increases in legal reserve requirements of member banks of the Federal Reserve System. For demand deposits the requirement of the central reserve city banks of New York and Chicago was lowered 2 points to 24 per cent. This had been advanced 6 points, in three steps, during 1948. The requirements of reserve city and nonreserve city banks were lowered 1 point in each case to 21 and 15 per cent respectively. These had been increased 2 points in September, 1948. For time deposits the requirement, uniform for all member banks, was shaved a half point, to 7 per cent. This had been raised 1½ points last September.

In connection with the reduction in reserve requirements Chairman McCabe of the Federal Reserve Board issued the following statement:

> The present action was taken in furtherance of the Board's policy of adjusting all of its credit regulations in accordance with changing economic conditions and the credit requirements of the current business situation. Since the first of the year there has been a decline of approximately one and one-half billion dollars in loans at member banks. About one billion of this decline has occurred at member banks in New York and Chicago — the central reserve cities. The remainder of the decline was largely at banks in reserve cities. In view of this trend of loans and the fact that requirements at the New York and Chicago banks had been increased from 20 to 26 per cent during 1948 the Board felt that it was appropriate at this time to reduce the requirements for the central reserve city banks somewhat more than for other member banks. We have frequently stated that credit regulations are not a one-way street. They should be tightened or relaxed as general economic conditions require.

Bank Loan Contraction

The drop in bank loans has been concentrated in the classification of business loans. The weekly reporting member banks, as the following table indicates, show a drop for this category of $1,814 million from the year end up to May 18.

Also noteworthy are the substantial levelling out in real estate loans and the decline in the category of "other loans" (including credit extended to consumers). The $273 million increase in security loans is associated with enlarged inventories of dealers in government and other securities. The $201 million rise in "other securities" held reflects enlarged bank absorption of State and municipal obligations.

Changes in Loans and Investments of Weekly Reporting Member Banks

(In Millions of Dollars)

	First 20 weeks of the year 1949	1948	1947
Business loans	—$1,814	—$ 428	+$ 511
Security loans	+ 273	— 100	— 709
Real estate loans	+ 27	+ 278	+ 405
Loans to banks	— 51	+ 128	+ 44
Other loans	— 74	+ 173	+ 149
"Other securities" (except U. S. Government)	+ 201	— 26	+ 26
Total loans and investments (except U. S. Government)	—$1,438	+$ 20	+$ 426
U. S. Govt. securities	+ 885	— 1,361	— 1,827
Total loans and invest.	—$ 553	—$1,341	—$1,401

Source of basic figures: Board of Governors of the Federal Reserve System.

The increase in the reporting member banks' investments in U. S. Government securities in the 1949 period is directly traceable to the use of funds released by the cut in reserve requirement percentages.

New Security Issues

Security flotations for the purpose of raising new capital show a slackening in comparison with last year, although the totals still run very large when compared with years previous to 1948. Tabulations by the Commercial and Financial Chronicle, summarized below, indicate that "new money" issues of corporations for the first four months of 1949 ran about one-sixth under the same period of 1948. Financing through new security issues still typically took the form of long-term bonds. The continued stalemate in the equity market is indicated by the fact that only $1 out of every $8 is being raised through the sale of common stock.

State and municipal flotations in the first four months were one-third under the January-April period of 1948 and one-quarter under 1947. The declines in this case are largely explained by huge veterans' bonus issues which came in the 1948 and 1947 periods. Borrowings by State and municipal governments to finance capital projects – such as highways and bridges and schools – are proceeding at a rapid rate.

New Security Issues for Purposes of Raising New Capital

(In Millions of Dollars)

	First Four Months 1949	1948	1947
Corporate			
Railroads	$ 199	$ 148	$ 60
Public utilities	659	832	323
Industrial & manufacturing	519	459	458
Oil	147	367	125
Other corporate	206	262	177
Total corporate	1,730	2,068	1,143
State and municipal	755	1,127	1,007
Total corporate, State and municipal	2,485	3,195	2,150

Source: Commercial and Financial Chronicle.

Bond Market Strong

In contrast to 1948, when the Reserve Banks bought government bonds so heavily to support the market, the shoe has been on the other foot this year and the authorities have been sellers of bonds to keep prices from rising too much. The change is the product of the slackening in private demands for credit, together with the reduction in legal reserve requirements of the member banks.

The recovery in bond prices – restrained by Federal Reserve selling with the objective of maintaining "orderly market conditions" – has cancelled out the "Christmas Eve" 1947 break in the bond market when the authorities lowered their fixed pegs on government bond prices.

On the rise in the market the Federal Reserve authorities have pursued a flexible policy, rather than adopting any fixed "ceiling" prices or pegs. Thus, while preventing sharp price run-ups, they have been in a position to control the amount of their selling. Total sales of bonds by the Reserve Banks since November 30, 1948, amount to $2.8 billion, a little over one-quarter of the $10.5 billion added to their bond holdings during the preceding thirteen months:

Federal Reserve Holdings of Government Securities

(In Millions of Dollars)

	Treasury bills	Certificates and notes	Bonds under 5 years to maturity	Bonds over 5 years to maturity	Total holdings
Holdings					
Oct. 31, 1947	$13,563	$7,897	$ 280	$ 428	$22,168
Nov. 30, 1948	5,176	6,849	1,959	9,222	23,206
Apr. 27, 1949	4,977	7,326	2,037	6,868	21,208
May 25, 1949	4,214	7,107	1,976	6,394	19,691
Changes					
Oct. 31, 1947 to Nov. 30, 1948	—8,387	—1,048	+1,679	+8,794	+1,038
Nov. 30, 1948 to Apr. 27, 1949	— 199	+ 477	+ 78	—2,354	—1,998
Apr. 27 1949 to May 25, 1949	— 763	— 219	— 61	— 474	—1,517

Source: Board of Governors of the Federal Reserve System.

The last line of the foregoing table reflects the heavy sales of securities the Federal Reserve Banks made to compensate for the reduction in member bank reserve requirements, effective May 1-5. As a result of these operations, the banks were able to put the funds released immediately to work, the greater part in short-term bills and certificates, and there was no abnormal accumulation of excess reserves, even temporarily. The experience put to rest apprehensions that, if reserve requirements were to drop again on June 30, through lapse of the special authority granted last August, a dangerous surplus of funds in the money markets might be created. The size of the Federal Reserve's holdings of government securities, still between $19 and $20 billion, is guard against such a contingency.

Treasury Financing

The securities market was treated to a surprise May 14 when the Treasury revealed its plans for handling June maturities of $4.3 billion in certificates and $1 billion in bonds. It had been widely expected that an offer might be made of intermediate-term bonds or notes, in view of favorable market conditions and the $26 billion of securities already scheduled to come up for refunding during 1950 in addition to $35 billion in the balance of 1949. Instead, holders of the two June maturities were offered one-year 1¼ per cent certificates in exchange.

The Treasury's offer, to be sure, fits the broad pattern of handling maturities during 1946, 1947, and 1948. Except where there was cash to pay off debt, one-year paper was generally offered in exchange. Nevertheless, it is recognized that conditions have changed. No longer has the Treasury excess cash balances and budgetary surpluses for paying down some of the maturing obligations. The floating debt (marketable issues maturing or first callable within one year) has been reduced since 1945 from $70 billion to $52 billion but it is still abnormally large, by any previous standard, in relationship either to the total debt or to any conceivable surpluses, and is now again on the increase. Moreover, in the next few years all of the ten-year 2 per cents sold during the war will come up for refunding.

That the responsible authorities have been and will continue to be weighing alternatives for handling nearby maturities was apparent in testimony presented by Secretary of the Treasury Snyder before the Congressional Joint Committee on the Economic Report last February. The Secretary called attention not only to $43 billion in marketable bonds and notes which fall due or become callable for redemption in 1950-52, but also to the $27 billion Savings bonds and notes which mature in the 1950-54 period.

At the same time Secretary Snyder presented projections of the cash needs of the Treasury which bear upon the more immediate position. He indicated that the Treasury would need—over and above revenues—$2.7 billion in the July-December period. On more recent appraisal, this estimate is too low. Revenues are falling short of the projections and Treasury cash balances, now around $3 billion, are $2 to $3 billion under the expected level at this time of the year and close to a prudent working minimum. Thus, for the first time since the Victory Loan drive back in 1945, the Treasury may have to return to the market as a borrower. This is a further reason for spreading the debt out and reducing the concentration in the next few years.

The Budget Crisis

During the past few months the federal budget outlook for the fiscal year beginning July 1 has been growing steadily worse. On the revenue side, the slump in business is requiring a downward revision in the estimates. Whereas the President, in his January budget, estimated revenues at $41 billion, tax experts of the Congressional Joint Committee on Internal Revenue Taxation now project the total at $38.9 billion, or approximately $2 billion under the President's figure.

Since the members of the committee are concerned primarily with revenues, the staff did not attempt to revise the expenditure estimates, but accepted the President's figure of $41.9 billion, as given in the January budget. On this basis, and allowing only for the expected drop in revenue, the committee experts anticipate a deficit approaching $3 billion for the year, instead of the $900 million indicated in the President's budget.

Comparison of Estimates on U. S. Government Finances for Fiscal Year 1950

(In Millions of Dollars)

	January Budget Estimate	Joint Com. Staff Estimate
Total budget expenditures	$41,858	$41,858
Total net receipts	40,985	38,900
Deficit	873	2,900

It now appears, moreover, that not only was the President's revenue estimate too high, but the expenditure estimate was too low. The latter did not allow for the cost of the Western European arms program, nor for other costs, which are looming larger than anticipated, such as agricultural price supports and veterans' benefits. According to Senator Byrd, total budget expenditures for the fiscal year are headed for more than $44 billion. This, in conjunction with the Congressional estimates of revenue, would mean a deficit of not $900 million but $5 billion.

An Alarming Trend

It is no wonder that thoughtful members of Congress are alarmed. Here we are with a prospective revenue total of $39 billion—about eight times that of 1939—and we still are unable to balance the budget!

Moreover, there is as yet no end in sight to this rising trend of government costs. The pressures upon Congress for more spending are terrific, and thus far the valiant efforts of a small group of economy-minded Senators and Representatives to cut major appropriation bills have, on balance, come to very little. Every attempt to reduce expenditures is met with loud cries of protest. The situation was well described by

Arthur Krock in the New York Times of April 24. Referring to the sources of resistance to economy, he said:

> A bureaucracy, entrenched in political patronage, is one. The military authorities, while conceding that there is some waste in their establishment, hotly deny the estimates of the Hoover Commission and point to the undeniable fact that security measures are wasteful in their very essence.
>
> The officials in charge of European recovery cry out that to make a percentage cut in their funds is to use an axe for a delicate surgical operation and kill a patient who otherwise will get well, and by his labors save the United States many more billions than any cut would save. Members of Congress, in turn, decline to make other savings by terminating or denying certain facilities to their states and districts – unneeded veterans' hospitals, for example.
>
> The effort to finance within the defense budget of $15.9 billion the military arms bill that is to follow approval of the North Atlantic pact meets the solid opposition of the Administration. The President will ask for a separate and additional appropriation which the Secretary of State recommends and the Secretary of Defense supports as a sum that cannot be subtracted from the national military appropriation without grave risks to security.

So it goes with every proposal for retrenchment. Meantime the budget gets bigger and bigger.

The Momentum of Spending

The table below, from a report on "Tax and Expenditure Policy for 1949" made public last month by the Committee for Economic Development, shows the tremendous momentum under which the spending program is operating. The figures cover total cash outlays by the Government, including not only expenditures charged to the regular budget but also disbursements from "trust accounts"; since these trust accounts are invested in government securities, the Treasury has to find funds to meet any cash drain either from tax revenues or by borrowing.

Changes in Federal Cash Expenditures, 1948-1950

(In Billions)

	Fiscal Years Actual 1948	Fiscal Years Proposed 1950 a	Change
TOTAL	$36.5	$46.3	+$ 9.8
Declining Programs b	6.4	2.6	— 3.8
Rising Programs	30.1	43.7	+ 13.6
Defense and foreign aid	15.5	21.6 a	+ 6.1
Veterans' life insurance dividends	—	2.0	+ 2.0
Farm price support	— .2	.6	+ .8
Social welfare c	3.2	6.2	+ 3.0
Resource development d	2.8	4.4	+ 1.6
All other e	8.8	8.9	+ .1

a Includes unofficial estimate of $600 million for military aid to North Atlantic countries, not included in Budget figures.

b Includes veterans' terminal leave payments, U. S. contribution to capital of International Bank and Monetary Fund, veterans' readjustment benefits, costs of surplus disposal, postal deficit.

c Includes following budget categories: Social welfare, health and security education and general research, labor.

d Includes following budget categories: natural resources not primarily agricultural, transportation and communication (except P.O.), agricultural except price supports.

e Mainly interest, general government, veterans' services not elsewhere specified, housing.

The main point to be noted is the way in which declines of $3.8 billion in certain expenditure programs (veterans' terminal leave payments, U. S. contribution to capital of the International Bank and Monetary Fund, veterans' readjustment benefits, costs of surplus disposal, etc.) are being more than offset by increases of $13.6 billion in programs which are expanding. The net effect is an increase of almost $10 billion in contemplated expenditures in 1950 over 1948, to a grand total of $46.3 billion.

While the budgeted payment of $2 billion for accumulated dividends on veterans' life insurance is largely a non-recurrent expense, the proposed broadening of the social welfare and resource development programs includes in many cases only very modest initial expenses of undertakings which may eventually cost billions. No one can foretell how much farm price support will actually cost.

The next table, from the Committee for Economic Development report, gives a breakdown of the budget totals for social welfare and resource development, and indicates the very substantial increases contemplated under all of the main headings. These large increases, be it noted, come at a time when the taxpayer is already carrying the heavy load of our enormously costly national defense and international aid programs, along with record costs for veterans, interest on the $250 billion national debt, and generally increased costs throughout the government establishment.

Increases in Expenditures for Social Welfare and Resource Development, 1948-1950

(In Millions)

	Fiscal Years Actual 1948	Fiscal Years Proposed 1950	Increase
TOTAL	$6,034	$10,628	$4,594
Social Welfare	3,213	6,228	3,015
Old age and survivors insurance program; total and permanent disability program; temporary disability program	559	2,245	1,686
Public assistance	733	1,129	396
Unemployment compensation	856	1,170	314
Federal aid to education	—	290	290
Railroad and federal employees retirement	466	594	128
Public health	146	284	138
Other	453	516	63
Resource Development	2,821	4,400	1,579
Highways, waterways, airways	963	1,435	472
Land and water (flood control, power, irrigation, reclamation, etc.)	493	951	458
Agricultural, except price supports	759	1,093	334
Atomic energy	475	725	250
Other	131	196	65

What Course of Action?

So long as the postwar business boom lasted, and the high tax rates produced a flood of Treasury revenues, it was easy to drift along and to postpone dealing with this problem of bringing the budget under control. The falling off in busi-

ness activity and revenues, however, has brought this problem to a head in a real budget crisis. The country now faces immediate decisions on three alternative courses of action.

One course is to increase taxes. This is the course advocated by the President. It will be noted, however, that not even a $4 billion tax increase such as he has proposed would cover the $5 billion deficit now considered by some experts as not unlikely. And more taxes would be bad both from the long-range view of placing new penalties upon enterprise, and from the short-range view of throwing an additional depressing load on business at a time when it is already declining.

A second alternative would be to follow the easy course of deficits and public borrowing. This, too, has strong arguments against it. Not only would it mean piling up more billions of national debt to burden us in the future, but its psychological effects would be harmful. To many people a revival of deficit financing at this stage would signify a budget beyond control, with all which that means in the way of threat to the soundness of money and the value of savings. Once deficit financing is begun, there is no telling where it will end. It may be recalled that the first deficits in the Roosevelt Administration were deprecated then as an undesirable but temporary condition, yet proved to be chronic and came to be embraced as a permanent method of "supplementing private investment" and "promoting full employment." An unbalancing of our budget now would come at a time when our representatives abroad, through E.C.A., are insisting on other countries treading the path of financial rectitude and putting their budgets in order.

The third way of meeting this budget crisis is by applying the common sense rule of good financial housekeeping and cutting down on expenditures. This can be done in two ways – (1) by eliminating some of the staggering amount of waste in government operations, revealed by the Hoover Commission. The President has asked Congress for authority to make administrative changes in the Government in the light of these findings and in the interest of efficiency. The Budget Bureau is quoted to the effect that more than a third of the recommendations of the Hoover Commission could be put into effect by the President without waiting for Congressional action.

(2) We might see what can be done about reducing some of the things we ask government to do for us, and particularly to concentrate on trimming new programs to which the country is not now committed. The truth is that the Federal Government is already trying to do far too many things at once.

To cut expenditures involves a willingness of everyone to consider his own pet projects requiring government outlays in the light of real national needs. Senators and Representatives complain bitterly against the frequency with which local organizations will write or telegraph a demand for balancing the budget one day, and then plead for federal aid to some local or national project the next.

The Committee on Public Debt Policy puts the problem of cutting government costs in a nutshell in its recently published book on *"Our National Debt – Its History and Its Meaning Today"** when it says:

> Cutting the budget is a political as well as an economic problem. Success depends on public opinion. Every budget cut hurts or inconveniences some person or some group, and a fight is put up against that particular retrenchment. An effective long-term program of government efficiency and reduction of unnecessary costs requires public education and support of sound policies.
>
> Reduction of government costs is not an easy nor a simple problem. It cannot be solved quickly. It calls for continued, vigorous effort and a united determination by the adminstration, Congress and the people to bring our Government to a higher measure of efficiency. Thus it may serve the people more adequately and at the same time will not be so expensive as to interfere with the country's economic well-being and retard its dynamic growth.

Long-Term Growth of Industry

With the publication of 1948 corporate reports now practically completed, it appears that the dollar output of American industry reached a new record of around $166 billion, exceeding the wartime peak of $154 billion in 1944 and almost three times the 1939 total of $58 billion. Much of the rise reflects, of course, merely the inflation of prices.

New high figures were established in total payments for wages and salaries, and in expansion and modernization of plant and equipment, financed in large part by the reinvestment of earnings.

The growth of industry in dollar terms over a long period of time is shown by the overall statistics of all U. S. manufacturing corporations as well as by the record of leading individual organizations.

It will be seen from the composite balance sheet and long-term chart for all manufacturing corporations (now around 98,000) that total assets increased from approximately $65 billion at the end of 1926, the first year for which official

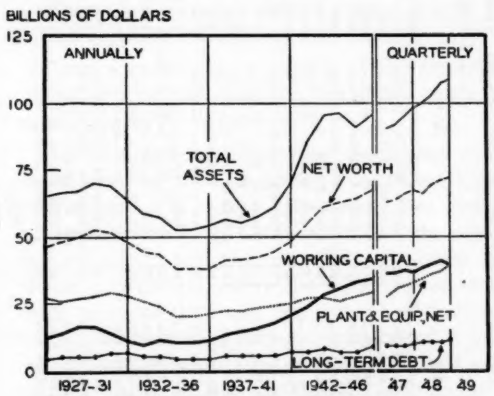
*Harcourt, Brace & Co., New York, 1949.

All Manufacturing Corporations in the U. S.
(In Billions of Dollars)

	December 31				
Assets	**1926**	**1939**	**1946**	**1947**	**1948**
Cash	$ 3.5	$ 4.6	$11.0	$11.2	$11.0
Government securities	1.8	1.2	7.2	6.8	7.1
Receivables, net	8.6	7.4	13.5	12.1	12.9
Inventories	12.3	11.0	23.3	26.5	29.7
Other current assets	*	*	*	1.4	1.3
Total cur. assets	26.2	24.1	55.0	58.0	62.0
Plant and equipment	*	41.6	59.2	*	*
Less depreciation	*	18.5	29.7	*	*
Net property	26.6	23.1	29.4	32.3	38.9
Other investments	11.9	8.3	9.4	*	*
Other assets		1.2	2.5	7.2	7.6
Total assets	64.7	56.7	96.3	97.6	108.5
Liabilities & Capital					
Accounts payable	3.2	4.8	9.2	7.7	8.1
Notes payable	4.0	2.2	3.5	2.8	3.0
Federal income taxes	*	*	*	7.1	7.7
Other liabilities	6.9	2.0	8.2	4.1	4.3
Total cur. liab.	14.1	9.0	20.9	21.7	23.0
Bonds and mortgages	4.3	5.3	7.9	8.8	11.0
Reserves	*	*	*	*	2.8
Capital and surplus	46.3	42.4	67.5	67.1	71.7
Total liab. & capital	64.7	56.7	96.3	97.5	108.5
Net working capital	12.1	15.1	34.1	36.3	39.0
Sales	62.2	57.9	139.0	150.7	165.6

*Not shown separately.

figures compiled by the Treasury Department are available, to $96 billion at the end of 1946. Subsequent quarterly estimates prepared jointly by the Securities & Exchange Commission and the Federal Trade Commission indicate a further increase in total assets to $108 billion in 1948.



All Manufacturing Corporations in the U. S.

Net working capital—current assets less current liabilities—rose from $12 billion at the end of 1926 to $34 billion at the end of 1946, and an estimated $39 billion by December 1948. In the years prior to 1939, working capital amounted to less than net property account. Since then the relationship has been changed by the rapid building up of the former, while the latter was held down by steady charges for depreciation reserves. During the past year, however, the heavy new investment in plant account has brought the two close together.

This great expansion since 1939 in volume of output and in total assets was accomplished without any impairment of working capital and with only moderate increase in long-term indebtedness. It was made possible by the substantial earnings during that period, a major portion of which was not paid out in dividends but was reinvested in the business. This provided additional equity capital to an extent that would have been impossible by the sale of new stock issues to investors in view of the restricted demand caused by high personal income taxes and other deterrents.

The relatively low figures at which plant and equipment are carried on the books, valued customarily at original costs less accrued depreciation, show for industry as a whole what many executives have emphasized in reports of their individual companies. Such book valuations are far below the costs of replacing the old plant and equipment as it wears out, which leads to an overstatement of real earnings.

For example, with a net property account for all manufacturing corporations carried on the books in 1946 at $29 billion, or only $2 billion larger than twenty years before, the value of goods produced was more than double. While the heavy additions to properties during the three years since the war, capitalized at the higher costs then prevailing, are a step toward adjusting book values in the direction of actual values, a large portion of the industrial plant is still greatly undervalued.

Industry Leaders in 1900

Turning to the long-term growth record of large individual companies, we find only a limited number of reports available at the beginning of the Twentieth Century. The population of the United States was only 76 million, and business was active following the depression of the 1890s and the Spanish-American war. American industry was in a vigorous youthful stage, but its ownership was, in contrast with today, so closely held that only relatively few corporations published reports.

In the first edition, dated 1900, of Moody's Manual, there were balance sheets of only 74 manufacturing companies reporting assets of more than $1 million each. Of this number 38, or more than half, were cotton mills, mostly located in Massachusetts and established in some cases as far back as the 1820s. The largest size companies were the iron and steel manufacturers, several of which in this and other lines represented consolidations made in the late 1890s. Many of the most important industrial consolida-

tions, however, were still to come in the early 1900s.

Among the leading industries of 1900 represented by companies in this investment manual, many of which were described briefly without either an income statement or balance sheet, were carriages, wagons, and bicycles, along with such lines as leather (tanning, shoes, belting, harness, saddles), brewing and distilling, ice manufacturing, tobacco, paper, pianos, phonographs, agricultural implements, railway equipment, gas fixtures and mantles, and cement.

In the non-manufacturing lines, there were prosperous railroad, traction, steamboat, and barge lines, and the start of an electric power and light industry. The manual listed many mining companies with colorful names but little information. There were as yet few signs of such giant modern industries as automobiles, aircraft, radio, petroleum, rubber, chemicals, plastics, rayon, motion pictures, etc.

The 25 largest manufacturing companies for which statements were published in the manual are given in the first column of the accompanying long-term table. These are not necessarily the largest in existence at that time, but merely the largest among those publishing balance sheets. Not only in 1900, but also in the subsequent years given, there may have been a number of other companies whose size would put them in the group of the 25 largest, but whose statements were not available.

Emergence of Other Industries

Between 1900 and 1910 the records reflect a substantial growth of industry, a great increase in availability of reports, and numerous important consolidations. The list of 25 largest companies in 1910 is headed by United States Steel Corporation, organized in 1901 by a merger including several companies that were in the previous list. Many other companies were forging ahead in the automobile, petroleum, rubber, and other newer industries, but had not yet attained large size or begun the publication of financial statements.

The industrial growth of the country during the ten years 1910-20, by which time the population had passed 100 million, was stimulated by the demands of World War I, followed by the rapid development of the automobile and petroleum industries. The growth in dollar assets reflected also the wartime inflation of prices. Among the companies entering the list were Ford Motor, organized in 1903, and General Motors, organized in 1908, as well as seven petroleum companies, some of which represented

25 Largest American Manufacturing Corporations, Based on Reported Total Assets at Beginning of Years 1900-49

(In Millions of Dollars)

1900		1910		1920	
Federal Steel Co.	$ 150	U. S. Steel Corp.	$1,822	U. S. Steel Corp.	$2,366
U. S. Leather Co.	137	Standard Oil Co. (1906)	372	Stand. Oil Co. (N.J.)	853
Am.Steel&W.Co.ofN.J.	106	American Tobacco Co.	286	Armour & Co.	491
Amer. Sugar Ref. Co.	102	Inter. Harvester Co.	173	Swift & Co.	490
Continental Tob. Co.	100	Amalgamated Cop. Co.	170	General Motors Corp.	447
National Tube Co.	94	Central Leather Co.	138	Bethlehem Steel Corp.	357
American Tobacco Co.	77	Pullman Company	131	Ford Motor Co.	333
Am. Smelt. & Ref. Co.	74	Armour & Co.	125	U. S. Rubber Co.	320
National Steel Co.	73	Amer. Sugar Ref. Co.	124	Stand. Oil Co. of N.Y.	300
Amer. Car & Fdy. Co.	69	U. S. Rubber Co.	121	Midvale Steel &Ord. Co.	280
American Woolen Co.	62	Am. Smelt. & Ref. Co.	119	General Elec. Co.	277
National Biscuit Co.	58	Swift & Co.	113	Inter. Harvester Co.	267
Internat. Paper Co.	56	General Electric Co.	102	Sinclair Con. Oil Corp.	265
Republic In. & St. Co.	51	Corn Prod. Ref. Co.	97	Texas Company	261
Amer. Tin Plate Co.	51	Amer. Car & Fdy. Co.	91	Anaconda Cop. Min. Co.	254
Glucose Sugar Ref. Co.	42	American Can Co.	90	Phelps Dodge Corp.	247
Amer. Writ. Paper Co.	41	Lackawanna Steel Co.	88	E.I. du Pont de N. & Co.	241
Amer. Steel Hoop Co.	38	American Woolen Co.	86	Gulf Oil Corp.	218
Am. Hide & Lea. Co.	36	West. Elec. & Mfg. Co.	85	Am. Smelt. & Ref. Co.	215
Swift & Co.	34	E.I. duPont Powd. Co.	75	American Tobacco Co.	206
Ten. C., I. & R.R. Co.	34	Republic In. & St. Co.	73	Transcont. Oil Co.	198
National Lead Co.	31	Va.-Car. Chem. Co.	72	Magnolia Petrol. Co.	182
General Electric Co.	30	Internat. Paper Co.	71	B. F. Goodrich Co.	176
Union Bag & Pap. Co.	28	Bethlehem Steel Corp.	69	Stand. Oil Co. of Calif.	174
Rubber Gds. Mfg. Co.	27	Amer. Locomotive Co.	69	Pullman Company	171
Total	$1,601	Total	$4,762	Total	$9,589

1930		1940		1949	
U. S. Steel Corp.	$2,286	Stand. Oil Co. (N.J.)	$2,085	Stand. Oil Co. (N.J.)	$3,526
Stand. Oil Co. (N.J.)	1,767	U. S. Steel Corp.	1,769	General Motors Corp.	2,958
General Motors Corp.	1,325	General Motors Corp.	1,707	U. S. Steel Corp.	2,535
Bethlehem Steel Corp	802	Socony-Vac. Oil Co.	930	E.I.duPont de N. & Co.	1,585
Anaconda Cop. Min. Co.	764	E.I.duPont de N.& Co.	858	Stand. Oil Co. (Ind.)	1,500
Ford Motor Co.	761	Bethlehem Steel Corp.	733	Socony-Vac. Oil Co.	1,443
Stand. Oil Co. of N.Y.	708	Stand. Oil Co. (Ind.)	723	Texas Company	1,277
Stand. Oil Co. (Ind.)	697	Ford Motor Co.	692	Gulf Oil Corp.	1,191
Gulf Oil Corp.	687	Texas Corp.	661	General Electric Co.	1,177
Shell Union Oil Corp.	662	Stand. Oil Co. of Calif.	629	Stand. Oil Co. of Calif.	1,075
Texas Corp.	610	Anaconda Cop. Min. Co.	588	Bethlehem Steel Corp.	1,029
Stand. Oil Co. of Calif.	605	Gulf Oil Corp.	523	Ford Motor Co. (1948)	1,026
E.I. du Pont de N. & Co.	542	AlliedChem.&DyeCorp.	405	Cities Service Co.	992
General Electric Co.	516	Inter. Harvester Co.	402	Western Electric Co.	786
Armour & Co.	452	Shell Union Oil Corp.	401	Un.Carbide & Car.Corp.	723
Sinclair Con. Oil Corp.	401	General Electric Co.	392	Sinclair Oil Corp.	710
Allied Chem.&DyeCorp.	388	Republic Steel Corp.	365	Westingh. Elec. Corp.	694
Inter. Harvester Co.	384	Kennecott Cop. Corp.	361	American Tobacco Co.	687
Western Electric Co.	373	Consolidated Oil Corp.	358	Inter. Harvester Co.	672
Union Oil Co. of Calif.	370	Un.Carbide&Car. Corp.	337	Anaconda Cop. Min. Co.	660
Un. Carb. & Car Corp.	354	Swift & Co.	312	Shell Union Oil Corp.	641
Swift & Company	351	Armour & Co.	303	Allied Chem.&DyeCorp.	597
Kennecott Cop. Corp.	338	American Tobacco Co.	291	Phillips Petroleum Co.	579
Inter. Paper Co.	333	Western Electric Co.	288	Kennecott Cop. Corp.	575
Pullman, Inc.	316	Aluminum Co. of Am.	251	Chrysler Corporation	541
Total	$16,792	Total	$16,314	Total	$29,179

former subsidiaries of the Standard Oil Company of New Jersey.

During the active and prosperous decades of the 1920s there was substantial growth in the size and output of the manufacturing industries, including not only the notable expansion of automobiles and petroleum, but also the rapid development of newer lines such as chemicals, aircraft, and radio.

The long-term growth of American industry was checked during the depression years of the 1930's. Assets of manufacturing corporations generally were reduced by deficits, as well as by liquidation of assets and debt, and, in many cases, by substantial writedowns of book valuations.

The 25 Leaders Today

During the nine years from 1940 to 1949 there were two periods of great industrial expansion: first, in producing the weapons and materials for winning World War II, and later in meeting the accumulated postwar demands for all types of consumers' and capital goods. Corporate assets were increased by heavy expenditures on new plant and equipment, and by an expansion in working capital for carrying larger inventories and receivables, reflecting in part the wartime and postwar inflation in prices and costs. This increase in assets was financed to a major extent by reinvested earnings, and to a minor extent by borrowings and by sales of new stock.

There were at the beginning of this year 141 manufacturing corporations reporting assets of more than $100 million each.

The 24 largest manufacturing companies given in our table for 1949, excluding Ford Motor Company which is a family corporation, are owned by approximately 2,751,000 shareholders, about half of whom are women. This of course includes duplication where the same person owns stock of more than one company, but does not include all beneficial owners where stock is held by trustees. The number of employees last year totaled approximately 2,090,000 and received an average compensation of $3,600. The total assets represented an average investment of $14,000 per employee.

Of the revenues from sales and other operations aggregating $29.8 billion, 8 cents out of each dollar was paid in taxes, 4 cents in dividends, and 6 cents was reinvested in the business for plant, equipment, and net working capital, while 82 cents went for direct labor and for purchases of materials, parts, and all other expenses.

Large Enterprise Common in U. S.

The business structure of the United States is made up of some 500,000 corporations and 3,400,000 individual proprietorships, partnerships, etc., excluding farming. In certain of the industries only large organizations can provide the huge capital investment required for mass production at low costs. In many other industries, the small units are able to maintain their position and to prosper year after year. Small companies supply countless materials, parts, and subassemblies to the large companies, some of whom have more than 10,000 suppliers, and in turn distribute most of the finished products to the ultimate consumer. In many other cases, small business sees the operation through from start to finish.

During the growth of American industry since 1900, the number of large corporations has increased manyfold, as shown in our table. Whereas a "billion dollar corporation" was unique in this or any other country when the U. S. Steel Corporation was organized in 1901, there are now 12 manufacturing corporations in that size class. In addition, there are six "billion dollar" railroads, six public utility systems, 20 banks, and 12 insurance companies, making a grand total of 56.

Even a "million dollar" company may properly be considered "big business." The official Treasury Department figures show 33,194 American corporations exceeding this size at the end of 1946. Since then the number doubtless has increased substantially.

If size be measured by volume of business rather than assets, there are 215 American manufacturing corporations whose sales last year exceeded $100 million each. It is hard to overestimate the dynamic quality these businesses give the economy. In addition to the large manufacturing companies, the United States has 44 retail and wholesale trade corporations with annual sales of over $100 million each, 27 railroads, 18 public utility systems, and 13 in other lines such as mining, motion pictures, air transport, etc.

Such vast business activity is made possible by the opportunity which the American system has given to enormously increase production and mass purchasing power by the investment of savings in power plants, railroads, factories, and labor-saving equipment of all kinds.

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